DATE 1-9-09

IB Informational
meeting



House Taxation Committee
January 7, 2009

**Total Corporate Income -Federal Income Tax Gross Receipts or Sales Cost of Goods Sold** Less: **Equals: Gross Profit** Plus: Dividends, Interest **Gross Rent Gross Royalties Capital Gains Supplemental Gains** Other Income Equals: **Total Income** 



#### **Federal Taxable Income**

#### **Total Income**

Less:

Compensation of Officers
Wages and Salaries
Pension, profit sharing plans, etc.
Employee benefit program costs
Repairs, maintenance
Bad debts
Rents and interest paid
Taxes and licenses
Charitable contributions
Depreciation, depletion

Advertising and other deductions

Equals:

**Federal Taxable Income** 

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## Montana Corporation License Tax - Starting Point



The starting point for Montana's Corporation License Tax is:



#### Federal Taxable Income (FTI)



Federal law controls all of the income and deduction items discussed previously



#### **Montana Additions to FTI**

- Montana corporation license tax included in FTI
- Other state, local, foreign and franchise taxes (based on income)
- Federal tax exempt (municipal) interest
- Contributions used to compute Montana's charitable endowment credit
- Other additions (e.g. extraterritorial income exclusion, capital loss carryover)



#### **MT Subtractions from FTI**



- IRC "Section 243" dividends received deduction
- Nonbusiness income
- Montana recycling deduction
- Other reductions (e.g. current year capital losses must be deducted in year incurred)



**Federal Taxable Income** 

Plus: Montana Additions

Less: Montana Subtractions

**Equals: Adjusted Federal Taxable** 

Income

Apportionment – General Approach

Corporations operating in more than one state must have their income apportioned to each of the states in which they operate.

Montana apportions income of multistate corporations using the traditional Uniform Division of Income for Tax Purposes Act (UDITPA) equally-weighted, 3factor apportionment formula.



The UDITPA three factors used to apportion income under this approach are:

- PROPERTY (Original Cost)
- > PAYROLL
- > SALES

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#### **Apportionment Factor -Example Example Calculation of Apportionment Factor** for Multistate Corporporation **Factor** Montana MT Factor Property Factor \$2,500,000,000 0.0892 \$223,000,000 **Payroli Factor** \$327,000,000 \$16,000,000 0.0489 Sales Factor. \$1,298,000,000 \$98,000,000 0.0755 0.2136 Sum of Montana Factors: Apportionment Factor (sum of MT factors divided by 3): 0.0712 10



**Adjusted Fed Taxable Income** 

Times: Apportionment Factor

**Equals: Apportioned MT Income** 

Plus: Income Allocated Directly

to Montana

**Equals: Montana Taxable Income** 

(before net operating losses)

#### **Net Operating Losses**

- In simple terms, a net operating loss (NOL) is the excess of deductions over gross income in any tax year
- Corporations may reduce taxable income in previous or subsequent tax years by carrying forward or carrying backwards net operating losses
- Net operating losses may be carried back for 3 tax periods
- Net operating losses may be carried forward for 7 tax periods



Montana Taxable Income (Before NOLs)

Less: Net Operating Loss Carryover

Equals: Montana Taxable Income (After NOLs)

Times: 6.75% (7% if "Water's Edge" Corporation)

Equals: Tax Liability Before Credits

Less: Tax Credits

Equals: Tax Liability After Credits

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# Tax (Refund) Due at Time of Filing

Corporations may owe tax or be due a refund at the time of filing:

**Tax Liability After Credits** 

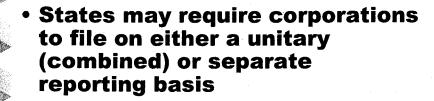
Less: Prior Year Overpayments

**Tentative Payments** 

**Quarterly Estimated Tax Payments** 

Equals: Net Tax (Refund) due





 Montana is a worldwide, combined unitary state and unitary corporations must apportion income as provided for in 15-31-305, MCA

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### Unitary (Combined) Reporting

#### **Business is unitary when:**

- 1) Operation within the state is dependent upon or contributory to operations outside the state, or
- 2) Units of the business within and without the state are closely allied or incapable of separate maintenance



Unitary requirements ("three-unities" test):

- 1) Unity of ownership (affiliate owned greater than 50%, control established)
- 2) Unity of operation (economies of scale centralized staff functions purchasing, advertising, human resources, etc.); and
- 3) Unity of use (centralized executive force making decisions regarding strategy and operations, intercompany transfer of products, know-how and expertise)

# Separate Company Reporting

- Each member of a commonly controlled group computes income and files a return as if it were a separate economic entity
- Provides opportunities to create legal structure and intercompany transactions to shift income from affiliates in high-tax states to affiliates in low-tax states



- Available only to multinational corporations
- Allows exclusion of corporations operating almost exclusively outside US (80% rule)
- Three-year renewable election
- Tax Rate of 7% (rather than 6.75%)

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### **Audit Program (RARs)**

- 15 Corporation Tax Auditors
- Desk Audits (RARs, NOL carry forwards, state adjustments, etc.)
- Field Audits (Review filing methods, large nonbusiness deductions, apportionment factors, etc.)